

Disclosure of Franchise Disputes

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Abstract:

The Amended FTC Franchise Rule requires franchisors to disclose material litigation and arbitration actions in Item 3 of their Franchise Disclosure Documents. The Amended Rule expanded the scope of the disclosure obligation so that most if not all franchisor-initiated actions must be disclosed in Item 3. As such, the Amended FTC Rule makes available both to franchisees and researchers information and data on franchise disputes, such as arbitration filings and proceedings and settlement terms, that otherwise would not be available.

Using the Item 3 data disclosed by Doctor's Associates, Inc., franchisor of the Subway sandwich shop franchise, this article finds that the frequency of franchisor-initiated actions in a state is, to a large degree, random. But it also finds a (weakly) statistically significant relationship between the frequency of disputes and the presence of a franchise termination statute, one that is negative in states with a low growth rate of Subway franchises but that becomes positive in states with a high growth rate. The Item 3 data thus provide a new perspective both on franchise disputes and the ongoing debate over the effects of franchise termination statutes.